


## Memorandum

To: Honorable Jerome E. Horton, Chairman  
Honorable Michelle Steel, Vice Chair  
Honorable Betty T. Yee, First District  
Senator George Runner, Second District  
Honorable John Chiang, State Controller

Date: May 11, 2012

From: Randy Ferris   
Chief Counsel

Subject: Other Chief Counsel Matters – May 30-31, 2012  
Item Number M - Request for Authorization to File *Amicus Curiae* Brief

*California State Teachers' Retirement System et al. v. County of Los Angeles*  
Second District Court of Appeal, Division 3, No. B225245  
(Los Angeles County Superior Court Case No. BC389742)

### **AUTHORIZATION IS SOUGHT TO FILE AN AMICUS BRIEF IN RESPONSE TO QUESTIONS POSED BY THE SECOND DISTRICT COURT OF APPEAL**

The purpose of this memorandum is to request Board authorization for the Legal Department to file an *amicus curiae* brief in the above appeal as requested by the Second District Court of Appeal in a letter to the Board of Equalization (Board) dated March 20, 2012. (See Attachment 1.)

**Issues Presented.** In this case, two principal issues are before the Court of Appeal: (1) Does the State Teachers' Retirement System (CalSTRS), which is exempt from property taxation and which paid the property tax assessed to its lessee, have standing to challenge the lessee's tax assessment; and, (2) if this court can reach the merits of the controversy, does Government Code section 7510, subdivision (b)(1) fail to tax a lessee's taxable possessory interest in accordance with the possessory interest's fair market value so as to render the statute's valuation methodology unconstitutional?

The trial court ruled against CalSTRS and in favor of the Los Angeles County Assessor (Assessor) on the second issue above. Now, the matter is before the Court of Appeal. It appears that the Court of Appeal has raised the standing issue on its own. The Court of Appeal has asked the Board to address a number of specific questions as they relate to the two principal issues before the court. (See Attachment 1, pp. 7-9.) Our response to these questions will be consistent with our recommendations on the two primary issues discussed below.

**Background Information.** The exclusive use or possession of publicly-owned real property by a private individual or entity is treated as a possessory interest and is subject to taxation. (Cal. Const. art. XIII, § 1; Rev. & Tax. Code, §§ 103, 104 & 107.) The fair market value of possessory interests is determined pursuant to the Board's Property Tax Rule 21 (Rule 21). In the case at issue, CalSTRS, a public retirement system, owns an office building at 924 Westwood Boulevard in Los Angeles in fee simple. Because CalSTRS is a public entity, its interest in the building is exempt from property taxation. (Cal. Const., art. XIII, § 3, subd. (a).) In January 1998, taxpayers entered into a five-year lease with CalSTRS for a retail space consisting of 1,280 square feet on the ground floor of the building. In a 2003 amendment to the lease, the parties extended the lease for an additional five years such that the lease terminated on February 4, 2008. The lease obligated the lessee to pay all property taxes imposed in connection with the leasehold.

Because the lease was for CalSTRS-owned real property, it created a taxable possessory interest in tax-exempt land. In valuing the lease which created the possessory interest, the Assessor applied Government Code section 7510, subdivision (b)(1), which states, in relevant part:

The lease shall also provide that the full cash value, as defined in Sections 110 and 110.1 of the Revenue and Taxation Code, of the possessory interest upon which property taxes will be based shall equal the greater of (A) . . . or (B) if the lessee has leased less than all of the property, the lessee's allocable share of the full cash value of the property that would have been enrolled if the property had been subject to property tax upon acquisition by the state public retirement system. . . . The lessee's allocable share shall . . . be the lessee's leasable square feet divided by the total leasable square feet of the property.

Applying the above provisions, the Assessor valued the possessory interest by taking the percentage of the total leasable square feet of the building subject to the lease and multiplying it by the factored base year value of the entire building. Using this methodology, the Assessor enrolled a value of \$418,618 for the possessory interest.

CalSTRS, however, argues that this methodology includes the value of its reversionary interest after conclusion of the lease term, which is in conflict with article XIII, section 3, subdivision (a) of the California Constitution and Rule 21, subdivision (b)(1), which states, in relevant part, that "the fair market value of a taxable possessory interest is the fair market value of the fee simple absolute interest reduced only by the value of the property rights, if any, granted by the public owner to other persons *and by the value of the property rights retained by the public owner.* . . ." (Emphasis added.) CalSTRS also argues that this assessment exceeds the fair market value of the interest held by the lessee in the real property, in violation of California Constitution, article XIII, section 1.

As further support for its position, CalSTRS cites Assessors' Handbook (AH) 510, which states at page 23 that: "the conventional approaches must be modified to accommodate the finite duration of a taxable possessory interest and the corresponding fact that a portion of the fee simple interest in those rights, *the reversionary interest, is retained by the public owner and is nontaxable.*" (Emphasis added.)

In summary, the Court of Appeal must weigh the provisions of Government Code section 7510 against article XIII, section 1 and section 3, subdivision (a) of the California Constitution, as well as Rule 21 to determine whether the Assessor correctly valued the possessory interest at issue.

As the Board lacks authority to declare a statute unenforceable or to fail to enforce a statute under section 3.5, article III of the California Constitution, the Board's published property tax guidance materials have referenced section 7510 despite concerns about constitutionality. But if an appellate court overturns the statute, then the Board's guidance materials will have to be corrected to conform to the decision.

### **Analysis of the primary issues before the Court of Appeal.**

**Issue No. 1: Standing.** As to the initial issue of whether CalSTRS has standing to seek a refund for property taxes that it has itself paid, but which it technically does not owe, we agree with CalSTRS that it has standing to seek such a refund despite the fact that their payment was "voluntary," and not "involuntary" in the common-law sense. While voluntariness used to be an issue, the California Supreme Court appears to have resolved the matter in *Franchise Tax Board v. San Francisco (Gonzales)* (2011) 51 Cal.4th 1006, where it held that: "Under our modern refund statutes, whether a tax payment was voluntary or involuntary is irrelevant. A taxpayer may seek a refund even without protesting the payment. This is a far cry from the common law right ... which extended only to payments extracted under compulsion." (*Id.* at p. 1017.)

### **Issue No. 2: Constitutionality of Statute.**

Section 7510 of the Government Code provides in pertinent part that:

#### **7510. Investment of assets in real property; payment of fee for general governmental services.**

(b) (1) Whenever a state public retirement system, which has invested assets in real property and improvements thereon for business or residential purposes for the production of income, leases the property, the lease shall provide, pursuant to Section 107.6 of the Revenue and Taxation Code, that the lessee's possessory interest may be subject to property taxation and that the party in whom the possessory interest is vested may be subject to the payment of property taxes levied on that interest. The lease shall also provide that the full cash value, as defined in Sections 110 and 110.1 of the Revenue and Taxation Code, of the possessory interest upon which property taxes will be based shall equal the greater of (A) the full cash value of the possessory interest, or (B), *if the lessee has leased less than all of the property, the lessee's allocable share of the full cash value of the property that would have been enrolled if the property had been subject to property tax upon acquisition by the state public retirement system.* The full cash value as provided for pursuant to either (A) or (B) of the preceding sentence shall reflect the anticipated term of possession if, on the lien date described in Section 2192 of the Revenue and Taxation Code, that term is expected to terminate prior to the end of the next succeeding fiscal year. *The lessee's allocable share shall, subject to the preceding sentence, be the lessee's leasable square feet divided by the total leasable square feet of the property.*

(Emphasis added.)

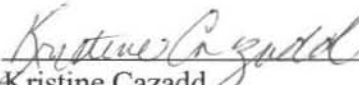
Section 1 of article XIII of the California Constitution mandates that real property be assessed at fair market value. There are only a few, narrow exceptions to this constitutional rule, and none are applicable here. Furthermore, because CalSTRS is a public entity, its reversionary or remainder interest in the building after expiration of the lease term is exempt from property taxation. (Cal. Const., art. XIII, § 3, subd. (a).) In addition, under the facts as given, the Assessor did not value the real property here in accordance with Rule 21, either as to the rights to be valued or the term of possession. Consequently, it appears that the property taxes paid were based upon an assessment that was in excess of the fair market value of the tenant's taxable possessory interest, and which included the value of the exempt reversionary interest held by the state agency.

**Recommendation.**

For the reasons stated above, the Legal Department asks for the Board's authorization to file an amicus brief that will respond to the Court of Appeal's questions in a manner consistent with the Board's historic understanding of the above-discussed provisions of the California Constitution as specifically reflected by the Board's interpretation set forth in Rule 21. It should be noted that such responses would generally support the arguments advanced by CalSTRS in this matter.

Should you require additional information or have any questions, please contact Assistant Chief Counsel Robert Lambert at (916) 322-0437 or Tax Counsel IV Richard Moon at (949) 440-3486.

Approved:

  
Kristine Cazadd  
Executive Director

RF:RL:th

Attachment 1: Letter from the Court of Appeal dated March 20, 2012

cc:	Ms. Kristine Cazadd	MIC: 73
	Mr. David Gau	MIC: 63
	Mr. Dean Kinnee	MIC: 64
	Mr. Robert Lambert	MIC: 82
	Ms. Christine Bisauta	MIC: 82
	Mr. Richard Moon	MIC: 82
	Mr. Daniel Paul	MIC: 82



JOSEPH A. LANE  
CLERK OF THE COURT/ADMINISTRATOR

DANIEL P. POTTER  
ASSISTANT CLERK/ADMINISTRATOR

## Court of Appeal

STATE OF CALIFORNIA  
SECOND APPELLATE DISTRICT

300 SOUTH SPRING STREET  
SECOND FLOOR, NORTH TOWER  
LOS ANGELES, CALIFORNIA  
90013  
(213) 830-7000

March 20, 2012

[SEE ATTACHED SERVICE LIST]

Re: *California State Teachers Retirement System v.*  
*County of Los Angeles*  
2d Civ. No. B225245  
(Los Angeles Super. Ct. No. BC389742)

Dear counsel and prospective amici curiae:

This appeal, which appears to be a case of first impression in California, involves the assessment of a taxable possessory interest, a leasehold, in tax exempt publicly owned real property.

There are two basic questions before this court: (1) Does the State Teachers Retirement System (STRS), which is exempt from property taxation and which paid the property tax assessed to its lessee, have standing to challenge the lessee's tax assessment? and (2), *if this court can reach the merits of the controversy*, does Government Code section 7510, subdivision (b)(1) fail to tax a lessee's taxable possessory interest in accordance with the possessory interest's fair market value so as to render the statute's valuation methodology unconstitutional?<sup>1</sup>

As is discussed below, it is the purpose of this letter to solicit from certain interested parties their views on those issues and to invite them to participate as amicus curiae in these proceedings. By way of assistance to those parties, the factual and procedural context in which these issues have arisen may be summarized as follows:

In 1984, STRS, a public retirement system, purchased the real property, an office building at 924 Westwood Boulevard in Los Angeles (hereafter, the building) for \$28.5 million. The building has approximately 143,377 in net rentable square feet. STRS owns the building in fee simple.

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<sup>1</sup> All further statutory references are to the Government Code, unless otherwise specified.

Because STRS is a public entity, its interest in the building is exempt from property taxation. (Cal. Const., art. XIII, § 3(a).)<sup>2</sup> However, a private lessee of publicly owned property is subject to property taxation on its possessory interest in the property. (§ 7510, subd. (b)(1).) Therefore, STRS's private lessees in the building are subject to property tax.

In January 1998, Dong Eil Kim and Chang Nim Kim, formerly doing business as Mail Boxes, Etc. (collectively, Kim or the Kims) entered into a five-year lease with STRS for a retail space consisting of 1,280 square feet on the ground floor of the building. In a 2003 amendment to the lease, the parties extended the lease for an additional five years, to terminate February 4, 2008. Kim's lease obligated Kim to pay all property taxes imposed in connection with the leasehold.

The County determined the base year value of the building based upon STRS's fee simple interest in the entire property. The base year was 1985 and the base year value was STRS's purchase price of \$28.5 million. The County trended the base year value forward a maximum of two percent per year from 1985 to 2006, pursuant to Proposition 13. (Cal. Const., art. XIIIa, § 2(b).) The cumulative upward adjustment from 1985 to 2006 was 48.642 percent. Thus, for the relevant tax year commencing July 1, 2006, the County assessed the value of the building at \$42,361,834. Of that sum, the County allocated \$29,744,119 to the office space and the remaining \$12,618,715 to the retail space in the building.<sup>3</sup>

The County established Kim's percentage of the total retail rentable square footage by taking Kim's square footage and dividing it by the total retail rentable square footage. The County determined Kim's premises represented 3.317437 percent of the total retail rentable square footage. Applying that percentage to the \$12,618,715 value of the retail space in the building, the County assessed the value of Kim's leasehold interest at \$418,618 for the tax year July 1, 2006 through June 30, 2007, shortly before the lease would expire. Based on the assessed value, the County levied property tax against Kim in the amount of \$4,983.34.

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<sup>2</sup> This exemption exists because allowing such property to be taxed "would produce the absurd result of having the state effectively tax itself. [Citation.]" (*L&B Real Estate v. Housing Authority of County of Los Angeles* (2007) 149 Cal.App.4th 950, 956.)

<sup>3</sup> These figures are taken verbatim from the summary judgment papers. There appears, however, to be a \$1,000 discrepancy in these figures.

STRS, which is constitutionally exempt from property taxation, paid the tax owed by Kim. STRS and Kim then filed an application with the County's Assessment Appeals Board (Board) to reduce the assessed value of Kim's leasehold interest and for a refund. Their application identified STRS as an "*affected party*" in the matter, and indicated the application was being presented as a "*test case*" to determine the appropriate valuation methodology for the various buildings STRS owns in Los Angeles County. The application challenged the constitutionality of Government Code section 7510, and further argued that even assuming the statute were constitutional, its provisions had been misinterpreted and misapplied by the Assessor.<sup>4</sup>

The Board denied the application. With respect to the constitutionality of section 7510, the Board ruled that, as a quasi-judicial body, it lacked jurisdiction to declare the statute unconstitutional. The Board further found the Assessor did not misinterpret or misapply the provisions of section 7510, subdivision (b).

On April 25, 2008, STRS and Kim (collectively, plaintiffs) filed a verified complaint in the superior court for refund of property taxes. They alleged in pertinent part: "The valuation methodology that the County Assessor used in making this assessment was unsound and did not properly apply the governing provisions of the California Constitution, statutes, administrative regulations and assessment procedures

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<sup>4</sup> Section 7510 states in pertinent part at subdivision (b)(1): "(b)(1) Whenever a state public retirement system, which has invested assets in real property and improvements thereon for business or residential purposes for the production of income, leases the property, *the lease shall provide, pursuant to Section 107.6 of the Revenue and Taxation Code, that the lessee's possessory interest may be subject to property taxation and that the party in whom the possessory interest is vested may be subject to the payment of property taxes levied on that interest.* The lease shall also provide that the full cash value, as defined in Sections 110 and 110.1 of the Revenue and Taxation Code, of the possessory interest upon which property taxes will be based shall equal the greater of (A) the full cash value of the possessory interest, or (B), *if the lessee has leased less than all of the property, the lessee's allocable share of the full cash value of the property that would have been enrolled if the property had been subject to property tax upon acquisition by the state public retirement system.* The full cash value as provided for pursuant to either (A) or (B) of the preceding sentence shall reflect the anticipated term of possession if, on the lien date described in Section 2192 of the Revenue and Taxation Code, that term is expected to terminate prior to the end of the next succeeding fiscal year. *The lessee's allocable share shall, subject to the preceding sentence, be the lessee's leasable square feet divided by the total leasable square feet of the property.*" (Italics added.)



in evaluating the Kims' possessory interest under the Lease ('the Possessory Interest'). Among other things . . . , 'assessing property tax on the full fee interest in the property rather than just the leasehold interest in the property' results in a differential taxation of real property that violates Article XXX, Section I of the California Constitution because the value taxed is greater than the fair market value of the lessee's possessory interest alone."

The complaint sought a judicial determination that: (1) section 7510 is void and unenforceable in that it violates the provisions of articles XIII and XIII A of the California Constitution; (2) the method of valuation used by the County Assessor and by the Board was unsound and resulted in an improper and arbitrary value for Kim's possessory interest in the premises; and (3) the common areas of the building do not constitute possessory interests subject to taxation because the common areas do not satisfy the requirements of possession, independence and exclusivity under the applicable law. Plaintiffs requested a refund of taxes paid and that the matter be remanded to the Board so that the County may value the possessory interest in a manner consistent with the trial court's determination.

Following cross-motions on summary judgment, the trial court granted the County's motion for summary judgment and took STRS's motion off calendar as moot. The trial court ruled on the undisputed "facts and given the relevant case law, the statute on its face and the valuation methodology as applied here has not been shown to be unconstitutional, violative of equal protection or arbitrary."<sup>5</sup> This appeal by STRS followed.

STRS now reiterates the arguments it raised below. STRS contends section 7510, subdivision (b)(1), violates the California Constitution because: (1) it does not value taxable possessory interests in accordance with their fair market value; (2) it taxes property exempt from taxation; (3) its classification of taxpayers violates equal protection; (4) its valuation methodology is not uniform in its application to all similarly situated taxpayers. STRS further contends the County violated the California Constitution in its application of section 75101, subdivision (b)(1) to Kim.

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<sup>5</sup> In granting summary for defendant County, the trial court ruled, inter alia: "It is undisputed that the Kims were only taxed for an amount equal to the actual square footage of their leasehold space at the subject property, there is no showing that the reversionary interest of STRS has been improperly included in that valuation." However, it appears that the County Assessor allocated the full value of the building, \$42,361,834, to the various lessees, without any reduction for the value of the reversionary interest of STRS/lessor.



Because of the broad importance of the issues presented, this court has vacated submission in this matter in order to invite amicus briefing from the State Board of Equalization (BOE), the California Public Employees' Retirement System, the Howard Jarvis Taxpayers Association, and other interested parties who may hereafter accept the court's invitation to participate as amicus curiae.

As noted at the outset of this letter, the two issues which are now before this court are (1) standing and (2) the proper interpretation and application of section 7510, subd. (b)(1).

As to the issue of standing, it is clear that the Kims, who are not parties to this appeal, lacked standing to sue because they did not pay the tax. (Rev. & Tax. Code, § 5140 [only person who paid the property tax may bring action for refund].) The standing issue raised in this case is whether STRS, which paid the tax assessed to its lessees even though STRS is tax exempt, has standing to prosecute the appeal? (See Rev. and Tax. Code, § 5140; *IBM Personal Pension Plan v. City and County of San Francisco* (2005) 131 Cal.App.4th 1291, 1304-1305; Rev. and Tax. Code, § 2910.7 [recognizing that agent may pay property tax on behalf of assessee]; 18 Cal. Code Regs., § 301(g) [party affected is any party having direct economic interest in payment of property taxes on the subject property]; Rev. & Tax Code, §§ 1603, 5097.) If the Kims lack standing because they did not pay the tax, and STRS, which paid the tax, lacks standing to sue, would anyone be able to raise the issue herein?

With respect to the section 7510 issue, there appears to be some confusion and inconsistency among various governmental bodies in the interpretation and application of section 7510, subdivision (b)(1). As a result, this court must decide whether section 7510, subdivision (b)(1), calls for the lessee to be taxed on the full value of the fee interest, *or merely on the value of the lessee's possessory interest*? If the statute is interpreted to require a lessee to be taxed on the full value of the fee interest, does the statute violate Equal Protection principles and/or Proposition 13, which bases the ad valorem tax on real property on the cash value of the assessee's real property? (Cal. Const., art. 13A, §§ 1, 2.) A corollary issue arises as to the precise definition of the term "possessory interest" and how it is to be calculated.

These issues appear to have laid dormant for two decades. This court recognizes that the BOE commented in 1992, at the time SB 1687 was under consideration, that "requiring the full value of the full fee interest to be assessed against a private lessee would amount to taxation of constitutionally exempt property. Accordingly, it appears that a constitutional amendment would be necessary to

accomplish the purpose of this bill.” (BOE, legislative bill analysis prepared July 7, 1992.) Also, the Enrolled Bill Report from the Governor’s Office of Planning and Research, dated September 2, 1992, stated “we do believe BOE has raised enough reasonable doubt about [SB 1687’s] constitutionality to question the wisdom of enacting this legislation at this time.” That report also noted the Assembly Republican Caucus’s position “that this bill may be unconstitutional because it may tax leaseholders at a higher rate than the fair market value of a leasehold estate and it would require leaseholders to make payments based on the ownership interest in the property even though the lessee holds only a possessory interest.”

The BOE has expertise in this area and therefore its view is entitled to some deference. Pursuant to subdivisions (c) and (e) of section 15606, it is the role of the BOE to “[p]rescribe rules and regulations to govern . . . assessors when assessing” and to “[p]repare and issue instructions to assessors designed to promote uniformity throughout the state and its local taxing jurisdictions in the assessment of property for the purposes of taxation . . . .” (*Hahn v. State Bd. of Equalization* (1999) 73 Cal.App.4th 985, 991, fn. 4.)

Toward that end, the BOE has promulgated Assessor’s Handbook, Section 510, Assessment of Taxable Possessory Interests, December 2002 (hereafter, Assessors’ Handbook) (available at [www.boe.ca.gov/proptaxes/pdf/ah510.pdf](http://www.boe.ca.gov/proptaxes/pdf/ah510.pdf)), and also has promulgated a regulation pertaining to valuation of a taxable possessory interest in publicly owned real property. (18 Cal.Code Regs., § 21(b).)

The Assessor’s Handbook takes the position that in taxing the lessee’s possessory interest, an adjustment must be made for the value of the reversionary interest retained by the public owner, which is nontaxable. The Handbook states in pertinent part at page 23: “TAXABLE POSSESSORY INTEREST VALUATION METHODS [¶] The valuation approaches for taxable possessory interests are similar to the conventional approaches to value—the comparative sales approach, the income approach, and the cost approach—that are generally accepted and used in the valuation of the fee simple interest. *However, the conventional approaches must be modified to accommodate the finite duration of a taxable possessory interest and the corresponding fact that a portion of the fee simple interest in those rights, the reversionary interest, is retained by the public owner and is nontaxable.*” (Italics added.)

Similarly, the BOE’s regulation pertaining to valuation of taxable possessory interests states in pertinent part: “(b) Rights to be Valued. Except as provided in subsection (f) or specifically provided otherwise by law, *the rights to be valued in*

*a taxable possessory interest are all rights in real property held by the possessor.* [¶] (1) The fair market value of a taxable possessory interest is not diminished by any obligation of the possessor to pay rent or to retire debt secured by the taxable possessory interest. In other words, *the fair market value of a taxable possessory interest is the fair market value of the fee simple absolute interest reduced only by the value of the property rights, if any, granted by the public owner to other persons and by the value of the property rights retained by the public owner (excluding the public owner's right to receive rent).*" (18 Cal.Code Regs. § 21(b), italics added.)

As already noted, it appears that, in this case, the County assessed the entirety of STRS' building at \$42,361,834, and then allocated that entire sum to STRS's lessees. As already noted, the County allocated \$29,744,119 to the office lessees and the remaining \$12,618,715 to the retail lessees in the building (including \$418,618 for Kim's retail space). *Thus, the County appears to allocate the entire valuation of the building to the various lessees, such as Kim, without any reduction for the value of the reversionary interest retained by STRS, the lessor, which owns the building in fee simple.* Further, it also appears that the County did not adjust the lessees' assessed value to exclude the value of common areas such as stairways, hallways, lobbies and elevators.

These circumstances raise a number of questions which the court requests that the amici should consider in addressing the two principal issues that are before this court:

(1) Did the \$418,618 assessed value of Kim's possessory interest exceed Kim's "allocable share of the full cash value of the property that would have been enrolled if the property had been subject to property tax upon acquisition by the state public retirement system" (§ 7510, subd. (b)(1))? In considering this question, please compare the position taken by County Counsel in this case with the following information and methodology set forth on the Los Angeles County Assessor's website (<http://assessor.lacounty.gov/extranet/overview/possint.aspx>).<sup>6</sup>

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<sup>6</sup> That website provides: "When a person or entity leases, rents, or uses real estate owned by a government agency for its exclusive use, a taxable possessory interest occurs. [Fn. omitted.] *The taxation of this interest is similar to the taxation of owners of privately owned property. However, a holder of a possessory interest frequently pays significantly less property tax than the private owner of a similar property.*" (Italics added.) Examples of taxable possessory interests include "Retail business operations in a publicly-owned building" (*ibid.*), such as Kim's business. With respect to methodology, the website explains: "Valuing Taxable Possessory Interest [¶] A base year value is established for taxable possessory interests upon a

2. It appears that the Los Angeles County Assessor included the value of the reversionary interest in valuing the Kims' leasehold interest. If so, did the County Assessor contradict its own guidelines and methodology, as set forth on its website? Further, is the instant interpretation by the County Assessor at odds with the BOE's interpretation and with the interpretation of other taxing authorities in California?

Here, County Counsel has argued: "[I]t is entirely reasonable that STRS's tenants *should expect to bear the same property tax burden* as other lessees of typical commercial real estate. . . . Tenants of STRS-owned property had no reasonable expectation of leasing such space at an effective tax burden less than that borne by lessees of privately-owned property, per the express terms of section 7510.) (Italics added.)

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change in ownership or completion of new construction under the guidelines of Proposition 13. [Fn. omitted.] This value, by law, will only increase by a maximum of 2% per year, until a new reappraisable event (change of ownership or completion of new construction) occurs, or the property suffers a decline-in-value. [¶] The valuation of possessory interests is different from other forms of property tax appraisal in two ways: [¶] 1. Only the rights held by the private user are valued. [¶] 2. *The Assessor must not include the value of the lessor's retained rights in the property or any rights that will revert back to the public owner (the "reversionary interest") at the end of the lease. [¶] As a result, possessory interest assessments are frequently less than the assessments of similar privately-owned property.*" (Italics added.) Said analysis, on the Los Angeles County Assessor's website, reduces the value of the possessory interest by the value of the public entity's reversionary interest in the property. The City of Newport Beach is in accord with this. ([www.newportbeachca.gov/Modules/ShowDocument.aspx?documentid=5209](http://www.newportbeachca.gov/Modules/ShowDocument.aspx?documentid=5209)).

See also the position taken by the Assessor in the County of Sacramento, to wit: "5. How are Possessory Interests Valued? [¶] The valuation approaches for taxable possessory interests are similar to the conventional approaches to value – the comparative sales approach, the income approach, and the cost approach – that are generally accepted and used in the valuation of a fee simple interest. *However, the conventional approaches must be modified to accommodate the finite duration of a taxable possessory interest and the corresponding fact that a portion of the fee simple interest in those rights, the reversionary interest, is retained by the government owner and is non-taxable.*" (<http://www.assessor.saccounty.net/GeneralInformation/TaxablePossessoryInterestsInPublicNon-TaxableProperty/default.htm#Answer5>.) It appears Sacramento's valuation methodology simply reiterates page 23 of the BOE's Assessor's Handbook.

However, as noted, the Los Angeles County Assessor has acknowledged on its website (<http://assessor.lacounty.gov/extranet/overview/possint.aspx>): “When a person or entity leases, rents, or uses real estate owned by a government agency for its exclusive use, a taxable possessory interest occurs. [Fn. omitted.] The taxation of this interest is similar to the taxation of owners of privately owned property. *However, a holder of a possessory interest frequently pays significantly less property tax than the private owner of a similar property.*” (Italics added.)

3. Is the disparity in taxation policy between publicly and privately owned property which is leased to tenants simply the inevitable outcome of the reality that the government/owner retains a reversionary interest which is non-taxable? Are there public policy implications arising from this circumstance, where it appears that a competitive advantage is realized by public owners over private owners of similar property?

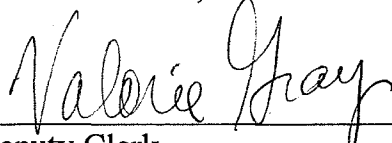
4. If section 7510, subdivision (b)(1) requires the lessee to be taxed on the unadjusted fee simple value of the real property, are the Assessor’s Handbook and the regulation (18 Cal. Code Regs. § 21(b)), both of which call for deducting the value of the reversionary interest, erroneous as contrary to statute?

5. Does the value of the lessee’s possessory interest decline with each passing year? Here, at the relevant time, i.e., the 2006-2007 tax year, the Kims had about one year remaining on their lease. The Kims’ monthly base rent was \$3,259. With the lease term approaching its February 4, 2008 expiration date, what would be the justification for assessing the value of the leasehold interest at \$418,618? Is that assessed value in excess of the fair market value of the possessory interest at that stage of the lease?

Prospective amici curiae are requested to advise this court at their earliest convenience as to whether they intend to file amicus briefs, and if so, the date the court can expect to receive the briefs. After the filing of the amicus briefs, the parties shall have the opportunity to respond thereto. (Cal. Rules of Court, rule 8.200.)

Yours truly,

JOSEPH A. LANE, Clerk

By   
Deputy Clerk

## SERVICE LIST

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